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Washington, D.C. 20505

MEMORANDUM FOR: Honorable Lionel H. Olmer
The Under Secretary for International Trade
United States Department of Commerce

SUBJECT: Commerce Department Study of Soviet/West European Pipeline Project

1. Thank you for sending me your analysis of the economics of the Soviet/West European pipeline. It is an excellent piece of work, treats the main issues systematically and contains considerable new information. I concur that more detailed information on specific contractual terms of equipment-supply and gas agreements must be obtained in order to complete and refine the analysis. Overall, the assumptions made are close to CIA's in most cases, but the range of uncertainty on some issues is still rather large. Specifically,

- o the estimate that European firms have charged 20 percent higher prices for goods and services for the pipeline is still a rough guess. CIA analysts believe that while the assumption may be accurate for West German goods, other countries may not have raised prices to the same extent,

- o the extent and level of interest rate subsidies is not well understood. The Commerce Department assumptions probably represent a high end estimate of the value of these subsidies, and

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William J. Casey

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UNITED STATES DEPARTMENT OF COMMERCE
The Under Secretary for International Trade
Washington, D.C. 20230

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MEMORANDUM FOR Honorable William J. Casey
Director, Central Intelligence Agency

FROM: Lionel H. Olmer

SUBJECT: Soviet/West European Pipeline Project

I am enclosing for your review the following analysis of the energy/economic elements of the Soviet/West European pipeline deal.

The primary finding of the paper is that the project appears to be commercially viable despite the interest rate subsidy the Europeans are extending to the Soviets.

The interest rate subsidy will be offset within five years by the higher prices (20%) the Europeans charge the Soviets for equipment and services and lower gas prices. Additionally, the price escalation and other commercial terms the Europeans received from the Soviets appear superior to comparable provisions in other Free World gas import transactions. The basis for the analysis is sensitive information obtained on the Soviet/Ruhrgas supply contract business proprietary from industry and foreign sources.

The information was difficult to obtain given the absence of a public natural gas regulatory process in Western Europe. The Europeans are also reluctant to divulge the salient price and cost terms of their transactions with the Soviets. My only concern is that we still need to obtain additional information on the specific loan and profit terms of European pipeline-related equipment and services contracts.

Attachment

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